right to participate in the profits and losses of Liberty as a going concern – in Liberty. Instead, the economic interest is held by the Liberty tracking stock shareholders.[28]

Similarly, the operation of Liberty's programming assets is conducted separately by Liberty's current management. A majority of LMC's board will be individuals who were on the LMC board prior to the AT&T-TCI merger (or will be selected by pre-merger incumbent directors) for seven years following the AT&T-TCI merger. The LMC officers and Board of Directors decide Liberty's course autonomously.[29] Liberty and AT&T can compete with each other in their lines of business and have no obligation to provide financial support, share corporate opportunities, or otherwise assist each other. Liberty has control over its financing capability and other corporate matters, and AT&T may not "unwind" its ownership of Liberty except by a spin-off to the Liberty tracking stock shareholders.[30] In sum, only Liberty's tracking

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[28] Many of the structural safeguards and infrastructure features that establish Liberty's economic independence have been included in the final judgment entered into with the Department of Justice in connection with the merger of AT&T and TCI (and therefore carry the imprimatur of law).

[29] The only exceptions to this rule are (1) in the context of disputes under the Inter-Group Agreement between AT&T and Liberty, which is governed by the contractual terms of the agreement, and (2) those limited matters that require action at the AT&T Board or committee level, such as the issuance of additional Liberty tracking shares. The scope of the Inter-Group Agreement is limited: The overall purpose of the Inter-Group Agreement is to provide that, to the extent possible (given that Liberty is owned, as a legal and tax matter, directly or indirectly by AT&T), the AT&T Common Stock Group and Liberty shall have no obligations or responsibilities to one another to provide financial support, to offer corporate opportunities, or otherwise to assist one another, except as set forth in the Inter-Group Agreement or in a separate "Intercompany Agreement" (which sets forth, among other things, a supply relationship between Liberty and the AT&T Common Stock Group as to programming services).

[30] For example, AT&T cannot increase the authorized number of shares of Liberty Group tracking stock or dispose of the Liberty Group's underlying assets without the consent of the Liberty Group tracking stockholders, and the proceeds of any issuance of Liberty tracking stock generally must be invested in the Liberty Group. LMC also has the unilateral right to authorize and issue new common and preferred stock, within specified limits.

shareholders have an economic interest in Liberty's programming investments and only Liberty's management has the right to direct the operation of those investments.[31]

AT&T, through TCI, also owns a non-controlling 33 percent equity interest in Cablevision Systems Corp. ("Cablevision"). By virtue of its interest in Cablevision, TCI has an indirect interest in Rainbow Media Sports Holdings, Inc. ("Rainbow"). Cablevision owns 75 percent of Rainbow,[32] which owns American Movie Classics, Romance Classics, Bravo, Bravo International, The Independent Film Channel, AMC Music Pop, MuchMusic and News 12 Network. Rainbow also owns 50 percent of National Sports Partners ("Fox Sports Net") and 60 percent of Regional Programming Partners, which owns several regional sports networks. TCI holds only Class A stock in Cablevision, each share of which has only 1/10th of the voting power of the Class B stock. TCI's voting interest in Cablevision is only approximately 8.9 percent. Although AT&T has the right to nominate two Cablevision directors, there are a total of 15 directors on the board, and a majority of the directors are elected by members of the Dolan family, or by trusts in favor of members of the Dolan family. Thus, Cablevison, not AT&T, controls the Rainbow programming services.

AT&T also owns a 50 percent interest in two cable partnerships with Time Warner Cable – Kansas City Cable Partners and Texas Cable Partners, L.P. Each of the partnerships has a management committee with six members, three appointed by Time Warner Cable and three by AT&T. However, Time Warner Cable is the general manager of the cable

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[31] Liberty also owns a 13 percent interest in General Instrument Corp ("GI"). As described above, Liberty is an operationally and economically distinct entity from AT&T. Therefore, AT&T effectively has no economic interest in, or right to direct the operations of, GI.

[32] NBC Cable owns the other 25 percent of Rainbow.

systems, with sole and exclusive responsibility for the day-to-day management and operations of those systems. Time Warner Cable has the right to take any actions it deems necessary or advisable on day-to-day activities, without obtaining the prior approval of the management committee. AT&T does not purchase programming or control programming decisions on behalf of the partnership systems. Rather, Time Warner Cable makes all programming decisions, subject only to compliance with the following specific requirements: it may not unreasonably favor Time Warner-affiliated programming over similar programming affiliated with AT&T; it must obtain AT&T's consent prior to deleting AT&T-affiliated programming; and, because of commitments made prior to the formation of the partnership, the partnership is required to carry American Sports Classics, Home Shopping Network, MSNBC, Romance Classics, The Box, and Web TV on the systems contributed by AT&T as soon as practicable. Thus, although Time Warner Cable may not unilaterally disrupt the carriage of certain existing programming on partnership systems, and although Time Warner Cable must add certain minimal program services to systems contributed by AT&T when practicable, AT&T has no ability to cause the partnerships to refuse to carry any particular programming service.

AT&T - Internet. AT&T began service as an Internet service provider in 1995, and began offering consumer dial-up access in early 1996 through the AT&T WorldNet Service ("AT&T WorldNet"). AT&T WorldNet, which currently has about 1.8 million customers,[33] focuses on providing Internet access to consumers. Although most consumers access WorldNet

[33] With its acquisition of the IBM Global Network ("IGN"), AT&T also obtained less than 300,000 additional non-corporate billed Internet subscribers in the United States. This number includes customers of other Internet access providers that use the IGN network to provide Internet access to their customers. For purposes of this Public Interest statement, AT&T has included all of these IGN-based customers in its WorldNet figures.

on a dial-up basis, connectivity is also available via Frame Relay or private line, at speeds ranging from 56 Kbps to 45 Mbps.

In its merger with TCI, AT&T acquired an interest in At Home Corporation ("@Home"), a Silicon Valley start-up founded in 1995, which provides content-enriched Internet access service over the cable television infrastructure.[34] AT&T offers the @Home service to its subscribers. The @Home service allows subscribers to connect their personal computers via cable modems to a new high-speed network developed and managed by @Home. Subscribers obtain access to the public Internet and to other online content, including content developed by @Home's @Media group, which aggregates content, sells advertising and provides premium services to @Home subscribers. @Home services were purchased by approximately 326,000 subscribers (including 74,000 AT&T customers) in the United States as of June 1999. AT&T holds a 25.9 percent equity interest and a 57.0 percent voting interest in @Home.[35]

MediaOne. MediaOne has operations and investments in two principal areas: domestic broadband cable communications and international broadband and wireless communications. MediaOne's combined revenues for 1998, both domestic and international, were approximately $7.1 billion.[36]

At the end of 1998, as described more fully below, MediaOne's domestic cable television systems passed approximately 8.5 million homes and provided service to

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[34] On May 28, 1999, @Home merged with Excite, Inc. The newly merged company is now called Excite@Home.

[35] Other entities holding an interest in @Home include Comcast Corp., Cox Communications, Inc., Cablevision Systems Corp., Kleiner Perkins Caufield & Byers, and Shaw Cablesystems Ltd.

[36] 1998 MediaOne Annual Report at 20.

approximately 4.97 million subscribers.[37] Over the past four years, MediaOne has invested about $4.1 billion in upgrading its traditional, one-way, analog cable plant to two-way, digital, high capacity broadband facilities. This upgrade is complete in about half of MediaOne's service areas. In 1998 and early 1999, MediaOne began offering facilities-based local telephone service to residential customers in seven metropolitan areas, beginning in Atlanta, Georgia and continuing to Los Angeles, California; Jacksonville and Pompano, Florida; Boston, Massachusetts; Detroit, Michigan; and Richmond, Virginia.[38] Despite these efforts, MediaOne's overall penetration rate for residential telephony service in the territories that it serves is less than 3 percent of the homes that it has upgraded to provide cable telephony. Currently, MediaOne has slightly more than 26,000 local telephony customers.[39]

MediaOne is not a competitive provider of long distance or international telecommunications services. Moreover, on April 6, 1998, MediaOne merged its domestic wireless mobile telephone businesses with AirTouch Communications, Inc. ("AirTouch").[40]

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[37] 1998 MediaOne 10-K at 1-2. MediaOne's interests in international broadband service providers passed approximately 2.6 million homes and provided service to approximately 993,000 subscribers. Among its international broadband interests, MediaOne holds a 29.9 percent interest in Telewest Communications plc, which provides cable and telecommunications services in the United Kingdom.

[38] 1998 MediaOne 10-K at 19.

[39] MediaOne also holds a 19 percent interest in Time Warner Telephone ("TWT"), a CLEC that provides local exchange and exchange access service, primarily to large business customers in urban areas. TWT serves approximately 20 cities, including four cities in New York (New York City, Albany, Binghamton and Rochester); three cities in North Carolina (Raleigh, Charlotte, and Greensboro); four cities in Texas (Dallas, Austin, San Antonio and Houston); two cities in Florida (Tampa and Orlando); two cities in Ohio (Cincinnati and Columbus); and San Diego, California; Memphis, Tennessee; Jersey City, New Jersey; Milwaukee, Wisconsin; Indianapolis, Indiana; and Honolulu, Hawaii. <www.twtelecom.com/TimeWarnerCities>.

[40] *See* 1998 MediaOne 10-K at 19.

This included MediaOne's 2.6 million domestic cellular communications customers, as well as its 25 percent interest in PrimeCo Personal Communications, L.P.[41] In exchange, MediaOne received a passive stock interest in AirTouch. AirTouch was acquired by Vodafone Group, PLC ("Vodafone"), on June 30, 1999, pursuant to the Wireless Telecommunications Bureau's Order released on June 22, 1999 consenting to the proposed transaction.[42] Through the consummation of Vodafone's acquisition of AirTouch, MediaOne's interest in AirTouch's mobile telephony business has been reduced to an interest in Vodafone of approximately 4.9 percent.

MediaOne - Cable Television Systems and Video Programming. MediaOne delivers a wide range of video products to homes and businesses, including: local broadcast stations; national, regional, and local cable programming services; premium movie and pay-per-view services; and sports programming services. As noted above, MediaOne's cable systems pass approximately 8.5 million homes and serve approximately 4.97 million subscribers. A list of these interests is contained in Appendix B.

In addition, MediaOne has a 25.51 percent interest in TWE, which provides cable service through cable systems that pass approximately 17.9 million homes and serve approximately 11.2 million subscribers nationwide. The remaining 74.49 percent interest in TWE is held by Time Warner, Inc. After the Merger, AT&T will have no right or ability to participate in the management of the TWE cable systems, including programming decisions

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[41] *Id.* at 15.

[42] *See* Memorandum Op. and Order, *In re Applications of AirTouch Communications, Inc., Transferor, and Vodafone Group, PLC, Transferee, for Consent to Transfer Control of Licenses and Authorizations*, DA 99-1200 (FCC June 22, 1999) ("*AirTouch-Vodafone*").

made with regard to those systems.[43] The TWE cable systems are managed on a day-to-day basis by Time Warner Cable. Time Warner Cable makes programming decisions for the partnership systems, subject to the direction of the TWE Cable Management Committee. Following the Merger, AT&T will not have *any* representation on the TWE Cable Management Committee.[44]

MediaOne also holds interests in the following programming services: Food Network, Sunshine Network, Music Choice, E! Entertainment, Viewers Choice, Speedvision, Outdoor Life, in which MediaOne holds minority interests, and New England Cable News and Fox Sports New England, in each of which MediaOne holds a 50% interest. MediaOne does not manage or have affirmative control over any of these programming services.

MediaOne - Internet. Media One holds an approximate 34.67 percent interest in an Internet joint venture, Road Runner,[45] that was formed in 1998. MediaOne offers the Road

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[43] MediaOne also holds an indirect 25.51 percent interest in HBO, Cinemax, and WB Network, and a 12.5 percent interest in Comedy Central and Court TV, each through its minority interest in TWE. As described below, MediaOne does not control TWE's programming operations.

[44] AT&T will have the right to appoint two of six TWE Board members. However, regarding the operation of the cable systems, the TWE Board is subject to the authority of the TWE Cable Management Committee, in which AT&T will not have any participation. Thus, AT&T's appointment of these Board members will not give AT&T the ability to control programming choices for the TWE systems.

[45] The Road Runner joint venture is operated by ServiceCo LLC ("ServiceCo"), which is owned by MediaOne, Time Warner, Inc. and its affiliates ("TWI"), Time Warner Entertainment-Cable ("TWE-Cable"), the Time Warner Entertainment-Advance/Newhouse Partnership ("TWE-A/N"), Compaq, and Microsoft. Compaq and Microsoft each hold a 10 percent interest in ServiceCo. The remaining 80 percent interest of ServiceCo is owned by MediaOne, TWI, TWE-Cable, and TWE-A/N through Cable HoldCo, a limited liability corporation. The ownership of Cable HoldCo is as follows: MediaOne has a 31.38 percent interest, TWI has a 10.70 percent interest, TWE-Cable has a 24.99 percent interest and TWE-A/N has a 32.93 percent interest. MediaOne's interest in ServiceCo (including proportionate share of interests held by TWE and TWE-A/N) is 34.67 percent.

Runner service to its subscribers. The Road Runner service is a digital, two-way interactive offering that includes broadband connectivity between a cable operator and a subscriber, access to the Internet, interactive content and programming, menus, navigational aids, electronic mail, access to newsgroups, a web browser, hosting, and other enhancements. As of April 1999, approximately 250,000 consumers (including approximately 125,000 MediaOne customers) purchased Road Runner services.

III. MERGER STANDARDS

As detailed below, the Merger will combine AT&T's strong brand and telecommunications expertise with MediaOne's "last mile" cable facilities, thereby expanding and accelerating the merged entity's ability to compete with incumbent LECs in providing local telephone services to residential customers. The Merger also will increase consumers' access to a wide array of packaged and *a la carte* services – including video and content-enriched high-speed Internet access.

In assessing the competitive effects of a proposed merger, the Commission now employs the same basic analytical framework articulated in *Bell Atlantic-NYNEX* and developed in subsequent Commission orders.[46] This framework includes an assessment of merger-specific

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[46] *See AT&T-TCI* ¶¶ 13-16; Memorandum Op. and Order, *Application of WorldCom, Inc. and MCI Communications Corp. for Transfer of Control of MCI Communications Corp. to WorldCom, Inc.*, CC Docket No. 97-211, ¶¶ 15-22 (FCC Sep. 14, 1998) ("*MCI-WorldCom*"); *AT&T-Teleport* ¶¶ 14-19; Memorandum Op. and Order, *MCI Communications Corp. and British Telecommunications PLC*, 12 FCC Rcd. 15351, ¶¶ 28-30 (1997) ("*BT-MCI*"); Memorandum Op. and Order, *In the Application of NYNEX Corp., Transferor, and Bell Atlantic Corp., Transferee, for Consent to Transfer Control of NYNEX Corp. and its Subsidiaries*, 12 FCC Rcd. 19985, ¶¶ 37-48 (1997) ("*Bell Atlantic-NYNEX*"). AT&T and MediaOne do not believe that it is necessary for the Commission, in determining whether this Merger is in the public interest, to conduct the searching competitive effects inquiry that the Commission first

(Continued . . .)

efficiencies that result in benefits to consumers and a competitive analysis that involves identifying the significant competitors (actual and potential) and evaluating probable competitive effects in each relevant market.[47] More specifically, the Commission considers general public interest benefits that will result from a proposed merger, including, among other things, the procompetitive effect that the merger will have on the quality and price of services provided to the public. The Commission then seeks to determine whether the merger will reduce competition either by enabling the combined entity to achieve unilateral market power or by reducing the number of competitors in any relevant market to a number that facilitates the competitors' collective exercise of market power through coordinated interaction. The Commission also seeks to determine if a proposed merger will be procompetitive, by enabling a competitor more quickly or efficiently to compete with a dominant firm or to serve as a stronger maverick in preventing coordinated interaction in furtherance of the collective exercise of market power.[48] Ultimately, the Commission weighs the probable benefits of the merger against potential harms to determine whether, balancing both competitive and general public interest concerns, the proposed merger would promote the public interest.[49]

(... Continued)
employed in *Bell Atlantic-NYNEX* in assessing a proposed merger of two incumbent local telephone monopolists. Nevertheless, AT&T and MediaOne have provided the *Bell Atlantic-NYNEX* analysis that supports the grant of the Applications.

[47] *Bell Atlantic-NYNEX* ¶¶ 37.

[48] *See id.* ¶¶ 37-61; *BT-MCI* ¶¶ 33-52; *AT&T-Teleport* ¶¶ 11-19; *AT&T-TCI* ¶ 16.

[49] *Bell Atlantic-NYNEX* ¶ 2.

IV. THIS MERGER WILL PRODUCE SUBSTANTIAL PROCOMPETITIVE BENEFITS THAT OUTWEIGH ANY CONCEIVABLE HARMS

A. The Merger Will Produce Benefits In The Provision Of Telephone, Internet And Cable Service

The Merger of AT&T and MediaOne will provide substantial procompetitive benefits and will serve the public interest. Like the Commission, AT&T is committed to ensuring that residential local exchange competition becomes a reality sooner rather than later.[50] In pursuit of that goal, AT&T has taken substantial risks in order to make local telephone competition a reality. AT&T has invested tens of billions of dollars of shareholder assets to acquire TCI and modernize its cable network in order to provide residential consumers with local exchange and exchange access services. AT&T's merger with MediaOne will expand and accelerate these efforts, bringing choice and the benefits of competition to millions more local telephone consumers.

This Merger, like the AT&T-TCI merger, also will "create greater customer choice among video- and content-enriched high-speed Internet access services."[51] Indeed, as discussed in detail below, AT&T's cable investments are *already* stimulating incumbent providers to offer new services and products to satisfy consumer demand that has long been ignored.

Telephony. More than three years after its passage, the competitive promises of the 1996 Act remain largely unfulfilled. Although competition for the largest business customers

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[50] *See AT&T-TCI* ¶ 48.

[51] *Id.* ¶ 147.

is beginning to develop in some urban areas, mass market residential and small business local exchange competition is virtually non-existent.[52] The reasons for this are obvious. The regulatory mechanisms intended by Congress to facilitate immediate local competition have either proven uneconomic (in the case of total services resale) or have been foreclosed by the ILECs' continued abuse of their bottleneck networks (in the case of access to unbundled network elements).[53]

There thus can be no question about the enormous public interest benefits of bringing local exchange competition to consumers who currently have no alternative to their incumbent local telephone provider.[54] It is likewise clear that cable telephony is the only short term prospect for broad scale local competition at the mass market level.[55] The AT&T-MediaOne transaction will accelerate the deployment of cable telephony, make cable telephony more competitive with incumbent services, and bring alternative choices to even more consumers.

First and foremost, just as the Commission found with respect to the combination of AT&T and TCI, the Merger advances the public interest because it combines two firms with complementary assets. "AT&T is one of only a few firms that currently possesses the

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[52] *Id.* ¶¶ 46, 146-47; *AT&T-Teleport* ¶ 46.

[53] Only 1.5 percent of ILEC switched lines were resold by competitive local exchange carriers ("CLECs"), while less than one percent of large ILEC lines have been provided as unbundled network elements, with ILECs in 12 states providing *no* unbundled loops to competitors. Trends in Telephone Service, at 9-2, 9-3 (CCB Feb. 1999) ("*1999 Trends*").

[54] *AT&T-TCI* ¶ 146.

[55] *Accord, id.* ¶ 48.

experience, brand name assets, and financial resources that are essential for quick and substantial entry into the retail residential local exchange and exchange access markets."[56] Likewise, the Commission has recognized that while cable companies possess important "last mile" assets, they "do not have the same kind of brand-name reputation and expertise with respect to telecommunications services" as AT&T.[57] Thus, by combining existing cable facilities with AT&T's strong telephony brand, sophisticated knowledge of marketing telephony services, and technical expertise in establishing and managing telephone networks, "the combined firm will be able to provide an alternative to the incumbent LECs' services for residential customers far more quickly and effectively than either could separately."[58]

The Merger will bring these same benefits to millions more consumers that AT&T cannot serve through TCI cable facilities. MediaOne has faced a number of obstacles in developing competitive local exchange telephony. Absent the Merger, these obstacles will continue to inhibit MediaOne's establishment as a viable competitor to ILECs. One such obstacle is MediaOne's lack of brand recognition and, accordingly, consumer confidence, as a provider of telecommunications services. MediaOne therefore will immediately benefit from AT&T's strong telephony brand. MediaOne's success in local telephony also has been hampered by its relative lack of telephone network management expertise, particularly as compared with its ILEC competitors. Additionally, MediaOne has not had access to the

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[56] *AT&T-TCI* ¶ 47.

[57] *Id.* ¶¶ 47-48.

[58] *Id.* ¶ 48.

telephone marketing and customer care service expertise maintained by most telephone companies, including its ILEC competitors and AT&T.[59]

Thus, although MediaOne has begun a roll-out of cable telephony, it has achieved only modest success. MediaOne today has only approximately 26,000 telephone customers, despite having invested approximately $4.1 billion to upgrade its system to provide additional services, including cable telephony.[60] In the areas where MediaOne has upgraded its broadband network, MediaOne is achieving a penetration level of less than 3 percent of the homes ready for its telephone service. Moreover, MediaOne has determined that, on its own, the company will be able, at best, to achieve only the most modest penetration levels in local telephone exchange and exchange access services in the next several years, and that it will not reach significant penetration for almost a decade.

The reasons for MediaOne's low telephony penetration and slow projected growth are straight-forward. Consumers are, understandably, reluctant to purchase basic telephone services from a company without an established reputation for providing reliable, high quality telephone service. As a new entrant, and a cable company, MediaOne has no established reputation as a reliable telephone service provider. For example, one recent national survey found that while 65 percent of consumers would consider switching to a long distance carrier for

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[59] As with all CLECs, another significant obstacle to entering local telephony service has been MediaOne's dependency on the ILECs for essential elements of its service. MediaOne has encountered serious and extensive problems with the ILECs in the areas of interconnection, number portability, access to new telephone numbers, access to wiring in multiple dwelling units, and access to ancillary services, such as directory assistance, support services, repair, and intraLATA toll service.

[60] MediaOne projected completion of the upgrade of most of its local networks by the end of the year 2000.

local service, only 19 percent would use a cable company.[61] MediaOne's own internal analysis likewise has shown that consumers view telephone companies in general, and AT&T in particular, as having a greater reputation for quality and service.

AT&T's established telephony brand will improve both the overall penetration level that can be achieved by MediaOne and shorten the time period in which that level can be achieved. In a recent assessment of telecommunication brand images, IDC/LINK reported that "AT&T received the highest consumer confidence ratings nationwide" and consumers selected AT&T as the company that they were most likely to use as their primary provider of telecommunications services (including local, long distance, and wireless).[62]

In addition, providing facilities-based telephone service is a highly complex endeavor, requiring not only sophisticated engineering expertise, but also organizational structures that are capable of quickly responding to consumer demands. While MediaOne has begun to develop these skills and knowledge, there is much it can learn from AT&T. For example, MediaOne will gain the expertise AT&T has developed in managing today's sophisticated telephone networks, including the integration of local, long distance, and international networks along with the integration of circuit switched and packet switched networks. Similarly, MediaOne will have access to AT&T's highly sophisticated telephone marketing and customer care expertise and organizational structures.

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[61] "Alternatives for Phone Service," USA Today, at A1 (May 13, 1999).

[62] *Residential Telecommunications Brand Image Assessment 1998*, IDC/LINK Report (July 1998).

The Merger also will accelerate MediaOne's deployment of a new, more efficient architecture for providing cable telephony. Currently, MediaOne's cable telephony network employs a standard hybrid fiber coaxial cable ("HFC") architecture that uses circuit switching technology. Packet switching, using IP technology, promises to reduce substantially the costs of providing local telephone services because circuit switches hold dedicated circuits open (and thereby make scarce capacity unavailable) during the duration of a phone call even when there is no information being transmitted. By contrast, packet switches can route multiple calls through the same channel as well as route the same call through multiple channels. Moreover, IP telephony will make it easier to integrate voice grade traffic with data networks, thereby eliminating the need to have multiple, redundant networks for the separate services.

As AT&T explained in the TCI proceeding, while AT&T has begun deploying circuit switches in its existing cable network in certain cases to initiate service immediately, it intends to transition to a packet switched network as soon as possible. Indeed, AT&T is in the advanced stages of developing and testing the necessary equipment to provide IP telephony. Thus, the Merger will bring the significant benefits of IP telephony to consumers in MediaOne's territories much sooner than if MediaOne were to try to deploy this architecture on its own.

Finally, the Merger will increase the strength of MediaOne's competitive telephony offerings because MediaOne will be able to access AT&T's existing network infrastructure. Through its acquisition of Teleport, AT&T has local facilities in a number of the same cities MediaOne's cable facilities serve. With those facilities, AT&T is able to connect some of its customers directly to its long distance network and thereby avoid ILECs' exchange access facilities and access charges. Moreover, AT&T is able to use Teleport's assets to interconnect to incumbent networks at end offices rather than at tandem switches, thereby

avoiding tandem switch and shared transport charges. In contrast, MediaOne has few transport facilities and must generally interconnect to incumbent networks through tandem switches (for both local exchange and exchange access calls). Hence, by enabling MediaOne to utilize AT&T's existing local infrastructure, the Merger will allow MediaOne to interconnect more efficiently to incumbent networks and thereby become a lower cost and more effective local competitor.

For its part, AT&T gains more from MediaOne than simply its last mile cable assets. Although AT&T's general telecommunications expertise will assist the speed and potency of MediaOne's cable telephony offering, MediaOne has developed a knowledge base that can be transferred to AT&T to enhance AT&T's ability to provide cable telephony on the TCI system. As discussed above, AT&T intends to upgrade TCI's facilities to provide IP-based cable telephony. However, in the interim, it will use the same circuit switching architecture that is currently being used by MediaOne. In fact, MediaOne already has upgraded about half of its systems to provide for the initiation of cable telephony and has started providing services in seven of its service areas. AT&T will benefit from MediaOne's experience in deploying these facilities and using them to provide local telephone service.

For example, HFC architecture requires all data and telephony users to share limited signal space through random allocation of space based on immediate demand. Moreover, there are significant differences (both in quantity and in variations) between upstream demand (traffic generated from the customer) and downstream demand (traffic carried to the customer). Ensuring that sufficient capacity exists in the network, while at the same time not investing in unnecessary capacity, is therefore a central issue in the management of cable telephone

networks. With the Merger, AT&T will acquire the experience MediaOne has gained in managing bandwidth congestion on its network.

AT&T can also utilize existing MediaOne facilities to "jump start" cable telephony on neighboring TCI facilities. In several regions of the country, including the Miami-Fort Lauderdale area, MediaOne cable systems that have been upgraded to provide cable telephony adjoin TCI systems that are in the process of being upgraded. This means that AT&T can connect the distribution hubs in the TCI system to MediaOne's existing, upgraded headend offices. Not only does this mean that AT&T will achieve greater efficiencies because it will not have to duplicate the headend equipment – such as the local switch, DC power supply, and the routers and servers used to connect to the Internet – but it will also enhance AT&T's speed to market, thereby allowing it to bring the benefits of local competition even sooner.

Beyond increasing the speed and competitiveness of AT&T's cable telephony, the Merger will increase the geographic scope in which AT&T can offer local service. Although AT&T's purchase of TCI will bring local telephone choice to millions of residential consumers in several major markets, the TCI transaction only gave AT&T access to customers in those cities where TCI actually has cable facilities. By acquiring MediaOne, AT&T will gain *immediate* access – and the ability to provide competitive, facilities based local exchange services – to millions of consumers in service areas where it currently has no facilities and cannot provide competitive local telephony offerings.

Finally, the Merger will create economies in providing local exchange services in competition with ILECs. As AT&T demonstrated in the TCI proceeding, enormous investment

is required to develop and deploy effective cable telephony facilities and services.[63] Deployment of cable telephony requires a large fixed investment in the development of engineering protocols and operating standards and practices; construction and furnishing of central offices, transport facilities and databases; hiring and training of installation and maintenance crews; and establishment and staffing of customer care centers. Similarly, the costs of marketing new services to residential consumers are substantial. The Merger will allow AT&T to spread such costs over a wider base.

In this regard, it is important to recognize the fundamental differences between ILECs and cable providers. Although completion of the Merger will give AT&T a "footprint" roughly the same size as an Ameritech-SBC-PacBell, AT&T for several reasons will begin with many *fewer* customers than such an ILEC. First, cable and telephone service have dramatically different penetration rates: on average, 94 percent for telephone and 65 percent for cable television. Thus, even when a cable company passes as many houses as a telephone company, it has almost 30 percent fewer customers. Second, as a new entrant into telephony, cable companies start with *no* telephone customers. Third, cable companies must expend enormous sums of money to research, develop and implement broad scale cable telephone networks while ILECs already have ubiquitous, working networks in place. Thus, to achieve the same economies of scale as, and to compete on an equal footing with, ILECs, cable companies must be permitted to achieve footprints as least as large, or larger, than these large ILECs.

Internet. Just as the Merger will provide economies of scale and scope that will allow the merged entity to provide competitive local telephone service more expeditiously than

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[63] *See AT&T-TCI* ¶ 147.

either entity could individually, the Merger also will expedite AT&T's ability to provide content-enriched high-speed Internet cable services.

First, the upgrades that are required to provide local telephone service over cable plant are also necessary to provide cable Internet services over these same facilities. By expediting the rollout of competitive local telephone services, the Merger also hastens the investments necessary for widespread deployment of cable Internet services.

Second, investment by AT&T will spur investment by competitors, and lead them to provide additional services and decrease their prices. The Commission has noted that investment in broadband facilities by cable operators and CLECs "appears to have spurred incumbent LECs to construct competing facilities."[64] Indeed, this appears to be the case in markets around the country, where ILECs have lowered prices and expanded coverage areas only in response to the entry of substantial competitors.[65]

Video. By enabling AT&T to offer packages of telephone, video, and data services on an expedited basis to millions of American consumers, the Merger will provide

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[64] Report, *Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996*, CC Docket No. 98-146, ¶ 42 & n.84 (FCC Feb. 2, 1999) ("*706 NOI Report*").

[65] *See, e.g.*, Mike Farrell, *PacBell to Lower DSL Rates in Calif.*, Multichannel News, November 23, 1998. In other markets where cable operators have initiated broadband service, the incumbent carriers quickly followed suit. For example, @Home launched service in San Francisco in September 1996 and San Diego in May 1997, and Pacific Bell followed in November 1997 and September 1998, respectively. *See Pacific Bell's ADSL-Internet Access Packages Now Available to 180 California Communities* <www.sbc.com/PB/NewsArticle.html?query_type=articlequery=19990901-01>. Likewise, after @Home launched service in Phoenix in May 1997 and Denver in June 1998, US WEST followed in January 1998 and June 1998, respectively. *See US WEST Launches Ultra-Fast DSL Internet Service in Twin Cities; Continues Roll Out* <www.uswest.com/news/051398b.html>.

additional motivation for ILECs and others to step up their efforts to provide competing video programming to end users. The Merger also will accelerate the development and deployment of digital cable technology on MediaOne systems. While AT&T has been a leader in deploying digital technology domestically, MediaOne generally has chosen to focus on increasing the analog capacity of its cable systems. The benefits of digital technology are well known to the Commission. Most importantly, digital technology greatly increases a cable system's capacity and allows the cable operator to bring many more services to consumers, including local and regional programs, niche channels that may be of interest to a small segment of the audience, minority programming, and other diverse services. Digital technology also benefits programmers by creating new opportunities for the distribution of their product.

Clustering. The Merger also serves the public interest by increasing clustering, which will produce pro-competitive efficiencies with regard to all services. As a result of this Merger and the exchange of cable systems with Comcast, AT&T will add network clusters in a number of important service areas. Clustering increases local management, fosters regional programming services, such as enriched local news and sports offerings, enhances compatibility of set-top boxes, lowers maintenance and operating costs, allows more efficient architecture and reduces per-customer marketing costs. Clustering further facilitates the offering of new interactive video services because smaller systems must otherwise bear the cost of either unused file server capacity or use smaller, less efficient servers. Clustering is also essential to the efforts of AT&T to compete with geographically concentrated incumbent LECs because clustering reduces the per-customer cost of providing local telephony. It is precisely for these reasons that

the Commission has concluded that clustering provides significant economic benefits to consumers that outweigh any conceivable harms.[66]

B. These Benefits Cannot Be Achieved Independent Of The Merger

These pro-competitive benefits cannot be achieved on the same scale or as expeditiously absent AT&T's acquisition of MediaOne. As noted above, although MediaOne has begun offering cable telephony in several areas, it has achieved only limited penetration to date and its marketing studies show that consumers remain strongly reluctant to buy telephone service from a cable company. By contrast, for the reasons explained above, combining the complementary assets of AT&T and MediaOne will greatly accelerate and strengthen MediaOne's cable telephony offering.

Similarly, without the transaction, AT&T would be required either to duplicate MediaOne's extensive facilities or to attempt to contract with MediaOne to allow AT&T to lease its facilities to provide cable telephony. The former is economically infeasible, and deprives the public of the benefits in cost reduction and efficiencies generated by the Merger. The latter, as explained below, is, at best, an imperfect solution that would result in much less substantial economic benefits than full integration.

Contractual relationships, even where feasible, are much less efficient than full integration when the parties are trying to deal with rapidly evolving technologies and service.

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[66] Fourth Annual Report, *Annual Assessment of the Status of Competition in Markets for the Delivery of Video Programming*, 13 FCC Rcd. 1034, ¶ 140 (1998) ("*Fourth Annual Video Competition Report*"); Second Report and Order, *Implementation of Sections 11 and 13 of the Cable Television Consumer Protection and Competition Act of 1992*, 8 FCC Rcd. 8565, ¶ 17 (1993) ("*Cable Ownership Limits Order*").

This is particularly true where, as here, there is technology and service *convergence* – no one can predict very far into the future what technologies and services are going to develop increased demand and what that means for efficient allocation of cable bandwidth. Without knowing the answers to these questions, potential joint venture partners have difficulty resolving how much bandwidth would be reserved for services to be provided by one joint venturer and how much bandwidth would be reserved for services to be provided by the other joint venturer.

An undefined arrangement in this area is highly problematic because of the large contract-specific investments that must be made early in the project. As noted above, rollout of cable telephony and other cable services requires large initial investments in research and development, licenses and permitting, acquisition of real estate and capital assets, installation of cable and customer premises equipment, marketing and advertising, and staffing of customer care centers. Many of these investments, once made, are contract-specific (they could not be redeployed elsewhere by a party that withdrew from the project) and sunk (they could not be recovered even upon termination of the project). The rapid growth and change in technology and demand for service, the convergence of services, and the high costs associated with initiating service efforts all impact negatively on contractual allocation of the broadband network, especially for new entrants competing against well-established competitors such as ILECs. Accordingly, the most efficient option – the one that promises the most benefits to consumers in the shortest time – is for AT&T and MediaOne to merge and let consumer demand and market forces determine how bandwidth should be used.

V. COMPETITIVE ANALYSIS

The product markets possibly relevant to an analysis of the Merger include: (1) local exchange and exchange access services; (2) domestic long distance services; (3) United States international telephone services; (4) wireless telephone services; (5) multichannel video programming distribution ("MVPD"); (6) video programming; and (7) Internet access.

A. Local Exchange And Exchange Access Services

Residential Telephone Services. The Merger will greatly enhance competition for residential local exchange and exchange access services by enhancing the ability of AT&T and MediaOne to provide facilities-based local telephone service to mass market customers. As the Commission has recognized, "incumbent local exchange carriers are the sole actual providers of local exchange and exchange access services to the vast majority of residential and small business customers in most areas of the United States."[67] In 1997, ILECs earned more than 98 percent of all local exchange and local exchange access revenues nationwide, with competition from CLECs generally focusing on large business customers in large urban areas.[68] In February of this year, the Commission estimated that ILECs still earn at least 95 percent of all local exchange and exchange access revenues.[69] Within the last year, the Commission acknowledged that, regardless of the development of some competition for the largest business customers, it could find little evidence of any actual competition to the ILECs with respect to the provision of

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[67] *AT&T-Teleport* ¶ 21; *see also AT&T-TCI* ¶ 46 (recognizing dominance of ILECs in the provision of mass market telephone service).

[68] *AT&T-Teleport* ¶ 24 n.80; *1999 Trends* at 9-2.

[69] *1999 Trends* at 9-1.

mass market local telephone service;[70] the merger of AT&T and TCI provided the only such hope.

AT&T and MediaOne taken together today provide only a tiny fraction of residential local exchange and exchange access service across the United States. AT&T has approximately 220,000 local telephone service customers throughout the United States, with almost all of those customers receiving resold local ILEC telephone service. While AT&T is in the process of upgrading TCI's cable facilities and initiating new facilities-based local telephone service in service areas like Fremont, California, AT&T has no more than 15,000 such customers in Fremont and San Jose, California; Arlington Heights, Illinois; Dallas, Texas; and Hartford, Connecticut. For its part, MediaOne currently has approximately 26,000 local telephone service customers in Atlanta, Georgia; Boston, Massachusetts; Jacksonville and Pompano Beach, Florida; Detroit, Michigan; Los Angeles, California and Richmond, Virginia. As these figures indicate, AT&T and MediaOne do not currently serve the same service areas or compete with each other in the provision of facilities-based local telephone service in any service area.[71] As a consequence, the proposed Merger will not result in any diminution of competition for local telephone service in the areas served by AT&T and MediaOne.

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[70] *AT&T-Teleport* ¶ 24 n.81. In February of this year, the Commission estimated that CLECs control less than 3 percent of the switched access lines nationwide, and that while CLECS are deploying fiber optic systems, they still only control approximately 11 percent of that capacity. *1999 Trends* at 9-1, 9-2.

[71] AT&T does provide a limited amount of resold local telephone service in Georgia, where MediaOne has initiated local telephony offerings. MediaOne, however, has approximately 5,000 customers in this service area, and AT&T is no longer marketing its resold ILEC local telephony.

Moreover, all of the relevant service areas are dominated by the ILECs, which have considerably more than 90 percent of the customers and revenue in the service areas where MediaOne and AT&T provide local telephone service. Each of the major ILECs with which the merged AT&T-MediaOne will compete has *millions* of customers in these areas. In Georgia, for example, AT&T and MediaOne together serve less than 15,000 local customers through facilities-based service and resale. BellSouth, by contrast, reported more than 4.15 million subscriber lines in Georgia as of the close of 1998, slightly less than 85 percent of all local telephone lines in Georgia.[72] Almost all of the remaining 15 percent of local telephone lines were held by other incumbent local telephone companies.[73] Thus, even where both AT&T and MediaOne have initiated some residential local exchange service, they remain very small, and face a dominant competitor, which has over 100 times as many customers.[74]

As discussed above in Section IV, instead of inhibiting competition, the Merger unquestionably will promote competition in the provision of local residential telephone service in areas where MediaOne has existing network infrastructure. As a result of the Merger, AT&T and MediaOne together will be able to provide more competitive facilities-based local telephone services to more consumers much faster than AT&T or MediaOne independently could provide such service.

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[72] *Trends in Telephone Service*, at 98 (CCB July 1998) ("*1998 Trends*").

[73] In 1997, 35 other independent local telephone companies reported approximately 700,000 additional lines in Georgia. *Id.*

[74] Moreover, as the Commission found in *AT&T-TCI*, cable companies like MediaOne have "no special incentives, assets, or capabilities" outside of their cable service areas that would ordinarily suggest that they would compete with AT&T's current cable telephony efforts in the provision of local telephone service. *AT&T-TCI* ¶ 45.